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SUBJECT: SCENESETTER FOR U/S NICHOLAS R. BURNS' VISIT TO  
URUGUAY

REF: VARIOUS DEPARTMENT EMAILS

Classified By: Ambassador Frank E. Baxter  
for reasons 1.4 (B) and (D)

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Summary and Introduction  
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11. (C) American Embassy Montevideo and I warmly welcome you, WHA A/S Thomas A. Shannon and the other members of your distinguished delegation to Uruguay. Your July 10-11 visit comes at an especially auspicious time: only three months after the historic POTUS visit and right on the eve of Secretary of the Treasury Paulson's economic and financial

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mission. The Uruguayans will be keen to learn your perspectives on U.S. foreign policy for the region and the rest of the world. Your presence will also offer an important opportunity to advance the bilateral agenda with Uruguay beyond trade by highlighting other key U.S. policy objectives. Uruguay's democracy remains strong and its economic recovery from the 1999-2003 financial crises seems generally assured. But Uruguay needs to invest more in its people and be persuaded to change the prevailing statist, commodity-based mind set so that it can face the global challenges ahead and become a knowledge-based society. Uruguay also needs to do more to enhance its security -- including closer cooperation with us -- and to take more decisive action on security issues in international fora. Many Uruguayans simply doubt that a major terrorist incident could ever occur here.

12. (C) Though led by a leftist government, Uruguay continues to share many of our basic values, and it remains an island of democratic stability and good governance in a frequently turbulent region. Uruguay also plays a pivotal role in Latin America, where a number of countries have perilously distanced themselves from the U.S. After Uruguay's historic political shift to the left in the October 2004 elections, the USG focused on engaging the initially wary Frente Amplio (FA) government through a dialogue on trade. In large measure, this approach was successful and helped to produce

our presently healthy bilateral relationship. The May 2006 visit by President Tabare Vazquez to the White House and President Bush's reciprocal visit to Uruguay in March 2007 symbolized mutual understanding at the highest levels. Almost unimaginable just two years ago, the visits also sent a powerful message to the region that the U.S. is less concerned with ideological labels than it is in working with governments who respect democracy, human rights and the rule of law.

13. (C) The contrast of Uruguay's solid democracy helps to highlight the fallacies of the populist regimes in countries such as Venezuela, Bolivia, Cuba, Nicaragua and Ecuador -- and to some extent Argentina. Vazquez's model appears to be Chile and he enjoys a privileged relationship with Chilean President Bachelet. A few months ago, a survey by the magazine "the Economist" rated Uruguay as the only country in South America to enjoy "full democracy." The GOU is seeking U.S. market access and investment, but it is vulnerable on energy supplies (to Venezuela) and remains very preoccupied about its pulp mill dispute with Argentina. Uruguay also faces a long-term demographic problem; a low birth rate (except among the poor) is exacerbated by the brain drain of mostly young people who emigrate abroad in search of jobs. To the extent that we can, we need to re-assure the Uruguayans that we are their friends, expose them to more modern economic and commercial ideas and try to encourage them to cooperate more assertively on issues of regional stability and security -- including counter-terrorism, counter-narcotics and mil-to-mil cooperation. Lastly, Embassy Montevideo recently completed its rightsizing exercise for the Department. By any objective measure, it is short on the "substantive" personnel needed to carry out USG policies through the kind of personal diplomacy and contact that this culture requires. In the same way, Uruguay receives

very little in terms of U.S. assistance. I would welcome any thoughts you may have regarding such resources issues, especially against the backdrop of Hugo Chavez' increasing assistance to Uruguay and other countries in the region. End Introduction and Summary.

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Background  
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14. (U) Uruguay is a small, stable, democratic nation of 3.3 million people, almost half of them residing in its capital, Montevideo. Once known as "the Switzerland of South America," it has long been one of Latin America's wealthiest and most egalitarian countries, with per capita GDP exceeding \$6,000 during periods of growth. However, a four-year recession, which ended in 2003, cut this figure nearly in half and lowered Uruguay's historically excellent socio-economic indicators. Uruguay's economy has been recovering well over the past three years, with GDP growth of 7 percent in 2006, in large part thanks to continued orthodox economic policies. GDP per capita is back to around \$5,800, and the GOU recently repaid its entire IMF debt early. Most observers believe that Uruguay seeks to emulate Chile's economic model. Vazquez and Bachelet, both physicians, enjoy a close relationship and common views on economic and social goals and the means to achieve them.

15. (SBU) Many Uruguayans were traumatized by the 1973-85 period of military dictatorship, when security forces committed serious human rights violations in their campaign against violent insurgents and their sympathizers. Some people blame the U.S. for indirectly supporting the region's military governments during the Cold War. Slick propaganda and declassified U.S. documents from the period are frequently touted by our detractors as "proof" of our involvement. The complex history of the dictatorship created heroes and villains for both the left and right. Some of the persons involved -- including former Tupamaro guerrillas -- are still active in politics today. The real and imagined lessons from the dictatorship period continue to haunt modern politics, including the Uruguayans' perceptions of the U.S., especially where the Global War on Terrorism, Iraq,

Afghanistan and Guantanamo are concerned.

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Social Factors in Economic Development  
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¶16. (C) Uruguay still needs to resolve its philosophical quandary between economic dynamism and socialist egalitarianism. Many elements for strong economic growth are in place. The traditional pillars of its economy -- farming, tourism and finance -- are all doing well, and foreigners are increasingly investing here. But four things hold Uruguay back. The first is that Uruguay is part of Mercosur, which now includes Venezuela. Mercosur has increasingly devolved from an imperfect customs union into a more political organization, with anti-American overtones. Uruguay might need the consent of its Mercosur partners if it were to negotiate a Free Trade Agreement (FTA) with the United States, though many here argue that no authorization is needed. Second, the current Frente Amplio government still harbors hard-line Socialists, Communists, ex-guerrillas and powerful trade unionists. While in the minority, these groups are nevertheless quite vocal and influential. Third, many ordinary Uruguayans seem content to leave large segments of their economy, including telecoms, power generation, oil imports and several banks, in state hands. Finally, Uruguayan culture still values professions that are not particularly useful or marketable in the global economy. Universities here graduate too many architects and lawyers and not enough IT experts, entrepreneurs and engineers. As with the labor unions, the Communists have considerable influence among the teachers and in education. Still, an educated population, strong respect for the rule of law, a comparatively low crime rate, and a good infrastructure make Uruguay one of the more attractive destinations in the region for foreign investment.

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Bilateral Relations: Key Issues  
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¶17. (C) Expanding the trade relationship and encouraging investment have been the foundation of our engagement with the moderate segment of the GOU. On May 4, 2006, President Tabare Vazquez met with President Bush in the Oval Office where both leaders agreed to deepen our trade relationship. After this meeting, a series of visits by USTR officials examined the possibility of FTA negotiations, but the discussions did not immediately bear fruit. Instead, DUSTR John Veroneau traveled to Uruguay to sign a Trade and Investment Framework Agreement (TIFA) on January 25, 2007. An FTA and Trade Promotion Authority (TPA) issues were discussed again during President Bush's visit to Uruguay in March 2007. While President Vazquez is sometimes hesitant to utter the words "Free Trade Agreement" in public, he and his administration have repeatedly stressed their eagerness to maximize bilateral trade. In private, they have made it clear that their objective is to negotiate an FTA with the U.S. You may wish to broach the subject of an FTA in your private meeting with President Vazquez. We advise against raising it with Foreign Minister Gargano, however, because he is clearly opposed to an FTA with the United States.

¶18. (C) Aside from trade, we also need to intensify bilateral cooperation in areas such as counter-terrorism, counter-narcotics, mil-to-mil cooperation, container security, border controls, the upgrade of Uruguay's civil aviation authority to Category 1, alternative sources of energy (especially wind, bio-diesel and ethanol), phytosanitary issues and science and technology cooperation. We also believe that investing in people, through more cultural exchanges and support to English language training programs can make a difference towards changing the socialist mindset in Uruguay.

¶19. (C) Following the POTUS visit last March, the NSC sent taskers to various agencies and bureaus for the purpose of strengthening our bilateral ties. We have made progress in several areas, notably bio-fuels cooperation, promoting

entrepreneurship and innovation, and phytosanitary issues. On June 10-13, Industry Minister Lepira and a group of leading entrepreneurs from Uruguay were invited by Commerce Secretary Gutierrez to the first Americas Competitiveness Forum in Atlanta. The GOU has offered to host a follow-up symposium on innovation, to be held in Punta del Este in April 2008. We also arranged for a visit by a high-level Uruguayan delegation to Texas A&M and North Carolina State University, two leading universities at the forefront of biofuels research. Promising cooperation agreements and work plans were reached with both universities, and with the University of Minnesota, to develop biofuels in Uruguay. As for phytosanitary issues, Uruguayan blueberries are close to being certified for export to the U.S., and there is progress on the certification of lamb and citrus.

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President Vazquez  
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¶10. (C) A practicing physician (every Tuesday), President Vazquez is a cautious and prudent man who is sometimes shy in international settings. He appears to style himself after Chile's ex-President Ricardo Lagos, and his mild leadership style sharply contrasts with the bombast of Venezuela's Hugo Chavez, Argentina's Nestor Kirchner and Bolivia's Evo Morales. Vazquez is also a pragmatist, and what he most wants for Uruguay is jobs, investment and growth. At home and abroad he has been caught between the competing demands of radicals and moderates in his own coalition, and he often faces a tremendous challenge to balance these opposing forces. His leadership style is predictable: he tends to stay above the fray and allow competing factions in the FA to debate an issue to exhaustion and then weighs in with a final

decision. Vazquez' adroit and pragmatic leadership, along with Uruguay's strong institutions and the basically conservative nature of Uruguayan society prevented the radical tilt some observers predicted during the 2004 electoral campaign. The contradictions between the radicals and moderates inside the Frente Amplio will probably have to be resolved if it is to win the 2009 national elections, since in the last elections the FA won only 50.1 percent of the vote. President Vazquez recently declared that he would not seek to modify the Constitution in order to run for a second term as President.

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Domestic Politics  
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¶11. (C) Vazquez and his coalition Frente Amplio (FA) government have been in power for over two years and have continued to receive high ratings. (June 18, 2007 "Interconsult" poll shows Vazquez with a 59 percent approval rating.) The moderates in his cabinet, especially Econ Minister Danilo Astori and Energy Minister Jorge Lepira, have also enjoyed favorable approval ratings and the President's confidence, and therefore they exercise considerable sway in foreign policy and the economy. The radicals within the FA coalition have challenged Vazquez more seriously than the two debilitated opposition parties (Blancos and Colorados) who ruled the country during the past century. Vazquez still relies on a relatively small cadre of experienced officials to get things done, including his cabinet-level Chief of Staff Gonzalo Fernandez. A key ally in domestic politics has been Agriculture Minister and ex-Tupamaro guerrilla leader Jose Mujica who, despite his violent past, has often countered the extreme ideologues on the far-left. (Note: Mujica is a possible Presidential candidate. His MPP faction represents about 38% of the Frente Amplio, but many Uruguayan's distrust his Tupamaro past. A recent poll shows a 38% approval rating for him among the Frente Amplio and 13% among non-FA respondents. End Note.)

¶12. (C) Vazquez has also been able to appease many of the far-left radicals when he addressed the human rights abuses committed during the "dirty war" period of the military dictatorship, uncovered the buried bones of disappeared persons, and prosecuted some of the perceived worst human

rights abusers. EconMinister Danilo Astori is another probable Presidential candidate. Because of his orthodox economic policies and his past rivalry with Vazquez, he is not well liked within the Frente Amplio, though his appeal outside it with swing voters is much greater than Mujica's. Astori's latest poll figures show a 28% approval rating among the Frente Amplio and 61% among non-Frente respondents.

¶13. (C) The opposition Blanco (Nacional) and Colorado parties are still recovering from their historic defeats suffered during the 2004 elections, when they received only 34% and 10% of the vote respectively. The likely presidential candidates in the next (2009) election for the Blanco Party are Senator Jorge Larranaga ("Alianza Nacional" faction) and former President Luis Alberto Lacalle ("Herrerismo" faction), though the latter has recently said that he will not run. For the Colorado party, Pedro Bordaberry ("Vamos Uruguay" group), son of incarcerated ex-President Juan Bordaberry seems to be the only viable candidate at this time, though former Presidents Julio Maria Sanguinetti ("Foro Batllista") and Jorge Batlle (Lista 15) cannot entirely be ruled out. Both opposition parties are betting on swing voters and that the Frente Amplio will remain vulnerable on high taxes and soft on crime.

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Foreign Policy  
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¶14. (C) Uruguay's foreign relations have historically reflected the efforts of a small nation wedged between two powerful neighbors to advocate self-determination, respect for human rights and the rule of law, the pacific settlement

of disputes, and economic cooperation. While Uruguay does not see eye-to-eye with the U.S. on many international issues ranging from Kyoto to Cuba to the war in Iraq, both countries value freedom and independence. Uruguay has always punched above its weight in foreign affairs, but the ideological divisions within the Frente Amplio also explain its sometimes ambiguous foreign policy over the last two years. For example, the anti-American, pro-Venezuelan Foreign Minister Reinaldo Gargano was virtually absent from all the substantive bilateral trade discussions with the U.S. He has also been a non-player in Uruguay's number one foreign policy concern: the long-running, serious dispute with Argentina over the construction of a giant pulp mill on a shared river.

¶15. (C) By far, the GOU's most serious foreign policy problem has been the severe bilateral dispute with Argentina over the construction of a Finnish-owned paper mill on a shared river -- not only because of soured bilateral relations with Uruguay's closest neighbor, but also because of the implications to foreign investment, an independent foreign policy, the influence of radical NGOs and relations with Mercosur. At \$1.2 billion, the plant's construction cost represents 6% of Uruguay's GDP and its operation is expected to generate exports worth 2% of Uruguay's GDP. It represents the largest Foreign Direct Investment in Uruguay's history.

¶16. (C) On the other hand, Argentine government officials, some inhabitants of the Province of Entre Rios across the river, and environmental activists claim the plant would harm fishing, farming, and tourist areas along the Uruguay-Argentina border. Argentina also claims that Uruguay violated the 1975 Uruguay River Treaty. Aspects of the case have gone before the International Court of Justice in The Hague and a Mercosur Tribunal, but Uruguay has sought little redress with the OAS. The U.S. voted to support the World Bank's IFC loan to the project. Protesters from Argentina have blocked bridges between Argentina and Uruguay off and on since December 2005 at great cost to Uruguay's trade and tourism revenues. The Uruguayans have felt bullied by Argentina's treatment and disappointed by Brazil's indifference. The pulp mill dispute is part of a schizophrenic relationship with Argentina, as Uruguay explores possible cooperation on an LNG facility and perhaps even nuclear power in the long term. The pulp mill dispute has indirectly (some would say ironically) contributed to



Uruguay's tilt towards the U.S.

¶17. (C) Uruguay's robust participation in international peacekeeping operations (PKO) can be partly explained by its dedication to and faith in international organizations. (Uruguay has the highest per capita contribution PKO among participants). Uruguay has also recently submitted a \$20 million democracy-building proposal to the State Department for a project in Haiti, where Uruguay has stationed over 1,000 of its peace keepers. We note that some senior GOU officials (Deputy Foreign Minister Maria "Belela" Herrera and Director General For International Cooperation Ambassador Raquel Rodriguez) have told us that they have discussed this project proposal with you and A/S Tom Shannon on separate occasions. The full text of the project has been sent to BSC and to the Haiti desk and has been translated into English.

¶18. (C) Unfortunately, Uruguay's enthusiasm for international PKO is not matched in other areas of security cooperation. For example, the GOU still does not wish to engage in UNITAS naval exercises and its borders are porous and unpatrolled in many areas. Uruguay's military enjoys good relations with ours, but the 1973-85 military dictatorship's human rights abuses still casts a long shadow on its reputation and budget. Equally disconcerting is the Foreign Ministry's apparent lack of interest in security-related demarches on UN Security Council resolutions, Iran, WMD proliferation, counterterrorism and the like. Embassy expects that so long as the Socialist Foreign Minister remains at his post, we will continue to experience minimal cooperation on these types of issues. Uruguay has a growing drug problem and would

like more counter-narcotics cooperation with the U.S., but past INL funding has ranged from minimal to none.

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The Economy, Trade and Investment  
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¶19. (U) Uruguay is a major agricultural producer. Agriculture and agro-industry account for 23% of GDP and over 75% of total exports. The major Uruguayan exports are meat (over \$1 billion this year), long-grain rice, dairy products, wool and soybeans. Forestry has surged over the last decade, due to favorable investment conditions and a favorable climate, where eucalyptus grows almost twice as fast as in the U.S. Uruguay does not import agricultural products but does import processed foodstuff. Uruguay applies a 6.6% average tariff on agricultural goods and does not impose any kind of import quota. There are no subsidies to agricultural production or exports. Given the importance of this sector for the economy, Uruguay has been active in bilateral and multilateral fora to push for trade liberalization, and U.S. agricultural subsidies are a hot topic. The GOU's trade policy on agriculture has generally been in line with Mercosur's policies, and Uruguay is a member of the G-20 group of countries calling for the elimination of agricultural subsidies. The GOU threatened last year to file a case with the WTO on U.S. rice subsidies, but Embassy intervention allowed for the opening of a bilateral dialogue instead, in an attempt to resolve the issue. Talks are ongoing, but the threat of an impending WTO case still remains on the horizon.

¶20. (U) Economy Minister Astori has been pursuing orthodox macro-economic policies on controlling inflation (6.4% in 2006) and promoting growth and investment. This has resulted in continued strong growth over the past couple of years, at 6.6% in 2005 and 7.% in 2006. The GOU has also paid off its debt to the IMF early and has regularly issued bonds on favorable terms in the international financial markets, thus lowering its debt service costs. The debt to GDP ratio was down to 71% at the end of 2006, from over 101% in 2004. Unemployment is now in the single digits for the first time in 5 years. The country risk stood at 159 points in May

¶2007.

¶21. (C) Still, Uruguay has a heavy debt burden and no known hydrocarbon deposits, so that Venezuelan oil and money

provide considerable temptation to boost the economy. Uruguay's state oil monopoly ANCAP recently signed a deal with Venezuela's state-owned PDVSA to help fund 24 percent of the cost of oil exploration in the Orinoco region of Venezuela in return for a proportional share of the resulting oil. Details of the agreement remain murky, and observers are skeptical if ANCAP can fund its end of the bargain or if the endeavor will result in significant gains for Uruguay. As for PDVSA's pledge, a year and a half ago, to fund a \$600 million refurbishing of Uruguay's refinery to allow it to process Venezuela's heavy oil, it still remains to be implemented. There is also much interest in natural gas from Bolivia, but delivery through the existing pipelines would necessarily have to pass through Argentina, and thus be subject to the vagaries of Argentine power needs. Venezuela has also invested in several failing firms in Uruguay and has promised to do more. So far, except for oil at preferential prices, much of Chavez's promises to Uruguay remain unfulfilled. The GOU has also been the most wary of the Mercosur countries regarding Venezuela's Banco del Sur project, though in late June, Uruguay decided to join in on the project, over the objections of Minister Astori.

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Comment  
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¶22. (C) Though Uruguay is unlikely to ever become a strategic partner of the U.S., it can be a valuable friend in a region that has significantly distanced itself from us in many instances. Over the last two years, we have been able to

build a remarkable level of confidence with President Vazquez through enhanced trade initiatives and other confidence-building measures. Now is the time to clearly define where we want our trade dialogue to lead us and if an FTA is our shared ultimate goal. It is also the time to engage Uruguay beyond trade to other areas of bilateral cooperation including, regional stability, security cooperation, incentives to private enterprise and investing in people. I believe that we can help Uruguay to make progress in these areas, but it will take time and resources.

Meanwhile, your visit serves as a very important building block for deepening our overall engagement with Uruguay. End Comment.

Baxter